HOUSING ALLOWANCE DESIGN:
AN EVALUATION FOR SLOVAKIA

M~ris Mi±elsons
Eugene Rizor
(Quadel Consulting Corporation)
Alberto Martini

with
Peter Tatian
Jaroslava Zapletalová

December 1996

UI Project 06251-061-00

The Urban Institute
Washington, D.C.

Prepared for

East European Regional Housing Project, Housing Finance Component
Project 180-0034
U.S. Agency for International Development, ENI/EUR/DR/H
Contract No. EUR-0034-C-00-2033-00, RFS No. 61

ABSTRACT

During 1995, the government of Slovakia took preliminary steps toward the design and implementation of a national housing allowance program. The government has not made a final decision on many elements of program design. This report documents the recommendations made by U.S. Agency for International Development consultants for the design of the housing allowance system in Slovakia. These recommendations address four key areas of concern for the Slovak government as it contemplates implementing the new social program. They include: 1) assessing the fiscal impact of moving towards full cost rent levels, 2) integrating a housing allowance as part of the safety net, 3) specifying the housing allowance formula and determining its maximum standard rent setting, and 4) investigating program implementation objectives.

TABLE OF CONTENTS

EXECUTIVE SUMMARY

The Ministry of Labor and Social Affairs asked the U.S. Agency for International Development (USAID) for assistance in the design and implementation of a housing allowance program in Slovakia. This report focuses on specific design issues of a housing allowance and is part of a larger technical assistance effort that included disseminating housing allowance information to policy makers and the public.

The proposed housing allowance for Slovakia is designed to protect households from paying an excessive share of their income toward housing costs and will, therefore, allow rent control to be relaxed for additional revenues for the maintenance, operation, and repair of housing. In general, this type of consumer-based subsidy pays the difference between what a household can afford for housing and standard shelter costs, including utilities. The basic formula for determining the size of the housing subsidy is given by:

$$HA = MSR - (r * Y)$$

When reading the formula from left to right, HA represents the housing allowance payment; the MSR represents the maximum standard rent (total housing costs including utilities); the “r” in the formula represents the maximum share of income a household should pay to cover their housing costs; and the Y represents gross household income.

Two key criteria for the design of the housing allowance program are equity and efficiency. This report addresses many issues related to these criteria and offers recommendations based on examples form other countries with similar programs. These recommendations address four key areas of concern for the Slovak government as it contemplates implementing the new social program. They include: 1) assessing the fiscal impact of moving towards full cost rent levels, 2) integrating a housing allowance as part of the safety net, 3) specifying the housing allowance formula and determining its maximum standard rent setting, and 4) investigating program implementation objectives.

Moving Toward Full Cost Rent and Utility Fees

State budget outlays and local revenues are extremely important considerations when designing a housing allowance. Because the government plans to incorporate the housing allowance into the safety net system, additional funds from the state budget will be allocated to the Ministry of Labor and Social Affairs as part of the costs of social support programs. On the revenue side, since the government intends to raise rents along with implementing a housing allowance, it is anticipated that municipal governments will experience an increase in funds from rent payments and communal service fees.

The housing allowance system will redistribute income by granting poorer households a subsidy to cover part of their housing expenditures. As rents and utility charges rise, all households will contribute more toward their housing costs. Over time, these charges can be increased to cover the full cost of providing housing and related services.

We developed the Housing Allowance Income Support (HAIS) simulation model to help the Ministry of Labor and Social Affairs quantify the fiscal effects of a housing allowance program; it shows the extent to which increased revenue from rents and utility services might offset expenditures for allowance payments. Three scenarios were examined.

The first simulation is based on Slovakia's population, their incomes, and housing costs for renters, co-op members, and homeowners as of 1994. Assuming that a household should spend no more than 20 percent of income for shelter and related services, about a fourth of all Slovak households would be eligible for allowances. If all eligible participated, housing allowance payments (excluding administrative costs) would amount to about Sk 132 million per month; the average household allowance would be about Sk 311 per month.

Increasing shelter and service charges other than heat to levels that would cover the estimated full economic cost of providing these housing services would cause allowance program costs to rise sharply, but by less than the gain in revenue from rent. In a second simulation, we found that doubling rents, co-op fees, and homeowner utility charges (except heat) would yield additional revenues of Sk 265 per month to the providers of housing and related services, but would require only Sk 241 million of allowance payments to maintain the 20 percent of income maximum housing expense for poorer families. The net fiscal gain (excluding administrative costs) would be Sk 24 million per month.

In a third simulation, we also doubled the price of residential heat, to a level that would roughly cover the full costs of supplying the heat while maintaining the same participation rate (50 percent) in the program. This move would increase the total revenue to providers of shelter and related services (including heat) to Sk 635 per month; allowance benefits would increase to Sk 536 million per month, so that the net fiscal gain would be almost SK 100 million per month.

Integrating housing allowances as part of Slovakia's safety net

As the government of Slovakia formulates plans to introduce a housing allowance it will need to address many issues related to its design and implementation. Some of the issues this report addresses are:

How should the definition of income used in the housing allowance formula be coordinated with that used for other means-tested benefits?

How should the *"household*" (that is, the group of individuals whose income should be considered together) be defined for the housing allowance?

Which *reference period* should be used to measure income? How should How the reference period chosen for housing allowance be coordinated with that chosen for other means-tested benefits?

Should the benefit paid under other means-tested programs be included in the income used to determine the housing allowance benefit? Alternatively, should the housing allowance benefit be considered in determining eligibility and benefits for other programs? In other words, how should the different programs be "*sequenced*"?

Should the personal component of the subsistence minimum be included in the housing allowance formula? What are the consequences of its inclusion in terms of the amounts of housing allowance benefits received by households of different sizes?

The draft law on Social Support (Ministry of Labor and Social Affairs) contains a very detailed list of items to be included in total income used for program eligibility determination. This list does not explicitly include income from assets--such as interest, dividends, and income from renting property. The fact that taxation of interest and dividends is done through direct withholding, and that this income is not reported in the annual tax return can certainly pose some difficulties, but it does not seem reason to omit such sources from total income.

For some social programs, the natural group of individuals seems to be the *nuclear family*, since raising children is the direct responsibility of parents, and the fact that there might be other adults in the house can be disregarded. The appropriate household definition, both to establish the MSR and to determine income, seems to be the group of all individuals *who are resident at an address.* This solution (the "all residents" solution) has two disadvantages: (1) it increases administrative costs, because in some cases the income verification put in place to determine child allowances is not sufficient; (2) with potentially more income recipients in the unit, the need for updating the benefit amount increases proportionally. Despite these minor disadvantages, we maintain that the household definition should include all residents living at an address.

Subtracting the subsistence minimum (used to determine eligibility for social assistance) from income alters the distribution of housing allowance benefits. Including the subsistence minimum or ZM(p) in the housing allowance formula has two major consequences: 1) the inclusion of ZM(p) requires much larger values of “r”; and 2) it can generate a different distribution of benefits across different types of households. The HAIS model can used to test the effects of subtracting out the personal component (versus the housing component) of the subsistence minimum from gross income in the housing allowance formula.

Social program sequencing has two types of consequences. The first one is budgetary or how sequencing will effect the overall budget as well as individual program outlays. Keeping all other parameters constant, will it cost more to have social assistance (basic income support) computed before or after housing allowances? Second, how with program sequencing effect the income distribution? Will certain groups--differentiated by size or type--benefit more from one sequencing than from the other?

Since housing allowances are considered part of social support system in Slovakia, the advantages of an "housing allowance first" solution is that eligibility for all social support programs would be established first, leaving social assistance to be the program of last resort. This would help keep the two systems separate. This position of prominence for housing allowances would presumable increase the participation in this program, and also create less disincentives for work because housing allowances through its formula "taxes" earnings at the rate equal to "r" in the housing allowance formula, while social assistance (because it uses preset income thresholds to determine eligibility) taxes it at a rate of 100 percent.

Given that housing allowances will be integrated into this system, the reference period for determining eligibility is the "tax year". However, this system has limited effectiveness in terms of its ability to help those in need when they need it. Moreover, savings in terms of administrative costs from extending this system to housing allowances depends to a large extent on the degree to which the population entitled to housing allowance will coincide with that receiving child allowances.

Determining the MSR in the housing allowance formula

The maximum standard rent (MSR) setting in the formula will affect which households are eligible for the program, the amount of assistance those households receive, and the total costs of the housing allowance program. Key considerations in establishing the MSR include:

- The MSR is based on appropriate standards that are unique to Slovakia.
- Adjustments can be made as necessary without extensive and costly analyses.
- the MSR should provide incentives that encourage appropriate levels of housing consumption.

The proposed formula-based housing allowance provides incentives for households to consume housing closer to the MSR. For example, lower income households that are over-consuming (i.e., occupying housing larger than provided for in the MSR) would have a financial incentive to seek less expensive housing in order to pay less of their income for housing. Larger households that are under-consuming housing could, with a housing allowance based upon the MSR, better afford larger dwelling units. Moreover, housing allowances would provide households the freedom to "shop" for housing that suits their needs in terms of size, cost, quality, and location.

Each variable in the housing allowance formula affects who is eligible and how much they will receive. Staff at the Ministry of Labor and Social Affairs appear to have established two of the three basic parameters for the initial implementation of the program. A definition of income (Y) for the housing allowance program has been proposed that is quite similar to the definition currently used to determine other social support benefits. In addition, the maximum share of income devoted to housing costs ("r" in the formula) has been set at 20 percent based on the HAIS model simulations. Therefore, the principal remaining element of the formula to be determined is the value of the MSR. The MSR is an approximation of typical housing costs for a unit that is big enough for a given household size.

A recent study of housing costs conducted by the research institute of the Ministry of Labor and Family Affairs, found that average overall housing expenditures do not vary greatly by tenure type but they do vary by their components. This makes it easier to adopt a single standard; but, even if there was greater expenditure variation across these tenure groups, we would recommend that consideration be given to a single standard for housing consumption based upon the expenditures for typical municipal housing differentiated by size.

Program Goals

There are several goals in designing an effective housing allowance program. The goals relate the two criteria used to evaluate program design--equity and efficiency. For example, the government will want the program to treat equally all households in similar circumstances. In addition, they will want the assistance payment to reflect as closely as possible the actual income of the household at the time the household is making its housing payments. In setting program parameters they will want to minimize errors in payments (and certainly the opportunity for fraud), but we also want to minimize administrative costs. When these goals compete, designers of the program are challenged to balance program objectives to achieve the purpose of the program.

INTRODUCTION

During 1995, the government of Slovakia took preliminary steps toward the design and implementation of a national housing allowance program. The government has not made a final decision on many elements of program design, but there is sufficient agreement on key points to allow initial consideration of some auxiliary program design issues and planning an implementation strategy. Some of the areas where key agreement has been reached are:

- The program will be administered through the Ministry of Labor and Social Affairs with eligibility determined by the District Offices of this Ministry.

- The program will be incorporated into the existing structure of the safety net and will count child allowances as income but will not count social assistance benefits in determining eligibility and the amount of the allowance.

- All households in municipal, cooperative, or family housing whose size and income make them eligible will be able to participate.

- The housing allowance will equal the difference between a standard expenditures for housing, which vary by household size, and a percentage of household income determined to be a reasonable contribution toward housing.

- The program will be designed and prepared during 1996 so that it is ready for implementation nationwide starting in 1997.

The Ministry of Labor and Social Affairs has asked the U.S. Agency for International Development (USAID) for further assistance in the design and implementation of a housing allowance program. This report focuses on the design of a housing allowance, and is part of a larger technical assistance effort that included disseminating housing allowance information to policy makers and the public.

Additional technical assistance was requested to program a computer simulation model designed to take into consideration Slovakia's unique housing circumstances and household characteristics to estimate the effects of various housing allowance design alternatives on the number of beneficiaries and program expenditures. This Housing Allowance Income Support (HAIS) model is also capable of simulating the number and program outlays (exclusive of administrative costs) of two other major social programs (child allowances and social assistance). In this regard, it serves as a valuable analytic tool for the government in not only social program design but also on its impact on local and state budgets.

Background

Because housing in the transition economies of Eastern Europe was long considered an entitlement, reforms--for political as well as social reasons--have proceeded more slowly than in other sectors of the economy.

Indeed, many countries in the region have been slow to privatize publicly-owned housing and even slower to raise rents.

The situation in Slovakia is no exception. The first nation-wide rent adjustment took place in 1992, twenty-eight years after rents were last set using household space norms and four apartment quality levels. Within the last five years, residential utility prices have risen faster than rent resulting in households having to pay more for utilities than they do on any other housing expenditures. This situation exists in spite of heating and electricity subsidies. In addition, the pace of housing privatization has been uneven throughout Slovakia, and slow when compared to some Eastern European countries.

Municipalities in Slovakia are under fiscal pressure to generate sufficient revenues to cover their expenditures for goods and services. As landlords of rental housing they incur losses through direct or indirect subsidies attributed to the operation and maintenance of their housing stock. Two recent government-sponsored studies indicate that the estimated economic (full) cost of multifamily rental units is about two to five times greater than revenues generated by existing rents. Rent increases will need to take place so that rental housing in Slovakia can be adequately maintained.

The government of Slovakia is currently promoting a housing policy that places greater emphasis on individual responsibility. A system of housing allowances will help the government to move away from costly direct government provision of housing towards private market solutions while still protecting the poorer population. Indeed, municipalities as well as the state could substantially reduce the amount of subsidies by introducing a well designed housing allowance. Under a housing allowance program, subsidies are paid to needy consumers of housing as opposed to producers of housing. Empirically, it has been shown that consumer-based subsidies such as housing allowances are more efficient and equitable means of providing housing solutions than direct production (e.g., public housing) or indirect (e.g., tax rebates) subsidy schemes.

USAID has promoted housing allowances throughout Eastern Europe as a cornerstone of its policy advice for reform in the housing sector. Since the breakup of the former Soviet Union and the collapse of communism in Eastern Europe, nine countries in Europe have adopted a housing allowance program (five with the assistance of USAID) and relaxed rent control. Reform was first initiated by Russia, where a successful housing allowance scheme was first adopted by numerous cities in 1992. This was soon followed by the Czech Republic in 1993, when a nation-wide housing allowance was made available for eligible renter households. In addition, Hungary, Poland, Ukraine, Belarus, and the Baltic States possess their own versions of a means-treated housing allowance combined with social assistance.[1]

The Proposed Housing Allowance for Slovakia

To protect poorer households from economic hardship while pursuing policies to relax rent controls to increase revenues for the maintenance, operation, and repair of public housing, we recommend that Slovakia implement a formula-based housing allowance. In general, this type of consumer-based subsidy pays the difference between what a household can afford for housing and standard shelter expenditures, including utilities. We also recommend that the allowance be available for all households irrespective of tenure status. For administrative efficiency, we recommend that this subsidy be incorporated into the existing structure of Slovakia's social safety-net

[1] Annex A of this report describes many of the housing allowance schemes implemented by Eastern European countries.

and be payable directly to eligible households through local social program offices. The central government should develop the program to ensure uniform rules and universal availability free from local political influence.

The basic formula for determining the size of the housing subsidy is given by:

$$HA = MSR - (r * Y)$$

When reading the formula from left to right, HA represents the housing allowance payment; the MSR represent the maximum standard rent (total housing expenditures including utilities); the “r” in the formula represents the maximum share of income a household should pay to cover housing costs; and the Y represents gross household income. The MSR can be calculated for each household using floor space norms that vary by household size multiplied by average (per square meter) rent, energy, and maintenance costs. Allowance payments decline as income rises (at a rate equal to “r”) and equal the MSR when a household has no income. The MSR and “r” in the formula would change over time as incomes rise and housing expenditures vary.

Two key criteria for the design of the housing allowance program are equity and efficiency. This report addresses many issues related to these criteria and offers recommendations based on examples from other countries with similar programs.

Structure of the Report

This report is divided into four sections. The first section shows how the Housing Allowance Income Support (HAIS) model can be used to test the impact of various housing allowance design features on the number of beneficiaries and program outlays. This section also analyzes the impact on municipal and state revenue of three scenarios depicting different combinations of rent and utility increases along with a housing allowance The second section addresses issues related to housing allowance formula design and its integration into Slovakia’s existing safety net. The third section explains the use of the maximum standard rent (MSR) in the proposed housing allowance formula and our recommendations for setting MSR levels. The fourth section of the report provides the reader with a framework to address various implementation issues associated with administering a new social program.

As a supplement to the report, there are two annexes. One annex (A) describes the various types of consumer-based housing subsidies used throughout the world, focusing on countries of Eastern Europe that have implemented a housing allowance. The other annex (B) provides the reader with detailed forms with information generated by the HAIS model for the three housing allowance scenarios described in section one of the report.

SECTION I

FISCAL IMPACT OF MOVING TOWARDS FULL COST RENT

Background

State budget outlays and future local revenues are extremely important considerations when designing a housing allowance. Because the government will incorporate the housing allowance into the safety net system, additional funds from state budget will be allocated to the Ministry of Labor and Social Affairs as part of the outlays for social support. On the revenue side, since the government intends to liberalize rents along with implementing a housing allowance, it is anticipated that municipal governments will experience an increase in revenue from rent payments and communal service fees.

In addition, the housing allowance system will redistribute income by granting poorer households a subsidy to cover their housing expenditures. As housing expenditures rise, those with higher income will contribute more towards housing costs. Over time, housing expenditures will more closely reflect the true cost (or the market price) of providing housing and housing services. Currently, on average, households in Slovakia devote about 12 to 14 percent of their income towards housing expenditures, with poorer groups like pensioners and young married couples paying closer to 25 to 30 percent of their income. With the imposition of rent control, subsidies are directed to those households that can afford to pay more for housing. Because of this price distortion, effective demand for housing is not expressed and the basis for a market-oriented housing sector is constrained.[2]

[2] Housing in Slovakia is distributed among three tenure groups; municipal rental units which comprise about 25 percent of the total stock; cooperative housing which comprise another 25 percent of the total housing; and family housing or owner-occupied housing.

This section of the report focuses on three Housing Allowance Income Support (HAIS) model scenarios that depict various combinations of rent and utility levels, and program designs. We use the model to analyze the likely budgetary impact of housing allowance benefits and additional revenues from rent and utility adjustments. We also show how these additional revenues will offset the explicit and implicit subsidies that local governments pay for the maintenance and operation of municipal rental housing.

On-Budget State Housing Subsidies

Ever since the velvet revolution, the amount of explicit subsidies directed to the housing sector, as a percentage of total government expenditures, has decreased. For example, in 1990, the Slovak Republic spent about Kcs 15 billion on a variety of programs promoting housing development and operating subsidies for state-owned housing. This amount represented about 8.4 percent of the total government budget. In 1994, the amount of subsidies in nominal terms was about Sk 6.7 billion or about 4.0 percent of total government expenditures.

Housing-related subsidies come in several forms. In 1994, about Sk 2.4 billion was spent on heating subsidies funneled through municipal budgets. Another Sk 2.1 billion was spent on interest rate subsidies that payed the interest rate difference between the pre-1990 price of borrowing for home purchase or construction on heavily subsidized terms and today's market rate. Premium payments for the two contract savings schemes initiated in 1993 make up the remaining major outlay (Sk 1.9 million). Subsidies for the operation and maintenance of rental housing were gradually decreased starting in 1990 and eliminated altogether in 1993.

Moving Towards Full Cost Recovery in Municipal Rental Housing

Municipal rental housing must conform to a national law that dictates rents levels (according to floor space) and amenity levels. Because of strict rent control, municipalities subsidize their residential housing by deferring services or redirecting resources from other sectors. Indeed, two recent government-sponsored studies have estimated that rents need to increase from four to seven times to meet the maintenance and operating needs of existing multifamily housing. Moreover, imposition of rent control has discouraged investment in housing and created a situation where the true demand for housing and housing services cannot be expressed.

Bzdúch (UEOS, Institute of Economics and Building Construction) devised a cost model in 1995 to estimate the economic costs of operating and maintaining residential housing. The model basically compares actual outlays to the economic costs of operation and maintenance, including depreciation. Despite conservative assumptions for economic costs and depreciation, his model shows that rent revenues have never fully covered the economic cost of operating and maintaining rental housing. Indeed, this disparity has grown over time such that rents, on average, would need to be raised from their actual levels by about four fold.

Another study commissioned by the Ministry of Construction in 1995 had similar findings. This study compared the operations of privately managed and municipally operated properties. The study found that private management companies were able to provide better services at a lower cost. Further, this study estimated that rent levels would need to be raised two to five times to cover the full economic cost of operating and maintaining rental housing.

Based on the findings from these two studies, we can compute the subsidy attributed to rental housing in Slovakia. Working under the assumption that net rent (floor space rent) for the average 64 square meter rental housing unit is Sk 320. To arrive at the amount of subsidies accruing to the rental sector we can multiply the difference between actual rent and estimated full cost rent by the total number of estimated housing units in the municipal inventory (451,000 units). By using a two fold increase in rent, this amounts to Sk 144.3 million per month or about Sk 1.73 billion per year subsidy. If we use the more liberal estimate of five fold increase between the actual rent and full cost rent levels, we estimate a subsidy of Sk 577.3 million per month or about Sk 6.93 billion per year.

These levels of subsidies are not sustainable for cash-strapped municipalities. In addition, the amount of crowns that are needed for capital repairs (e.g. new roofs, plumbing fixtures, etc.) have not been taken into account. Over time, the cumulative impact of differed maintenance reduces the value of Slovakia's capital stock.

The implementation of housing allowances will facilitate rent increases in municipal housing. Higher rents will provide municipalities additional revenue for the operation and maintenance of rental housing, and will reduce the need for some municipalities to subsidize their rental housing by using other funds such as heating subsidies granted through the state budget.

An Overview of the Housing Allowance Simulation Model

The HAIS model was developed to assist the Ministry of Labor and Social Affairs determine program parameters and quantify the effects of a housing allowance system. The output from this computer-based simulation model includes the number of households that would receive income support through social assistance and child allowances. The user can perform sensitivity analyses by changing key program parameters for any of the three social programs it simulates.

A simulation model is only as good as the data with which it is supplied. The HAIS model uses the best and most up-to-date sample data available in Slovakia. Its base data file was constructed using data from the 1992 Microcensus survey. This file contains detailed data on the demographics, location, and income of households living throughout Slovakia. For the 1992 Microcensus, the Slovak National Statistics Office (NSO) devised a "housing" supplement to obtain information on unit size, location, and housing expenditures. The monetary components of the file were adjusted for inflation by statisticians at INFOSTAT, an independent branch of the NSO, to reflect estimated 1994 values.

For each simulation the model calculates household income over a user-specified period by updating earnings, pensions, and social benefits. The model also calculates housing expenditures according to assumptions supplied to the model about anticipated increases in rents and residential utility expenditures. The simulation's start date corresponds to the base data (fourth quarter 1994) while the end date of the simulation is user-specified (month and year). The HAIS model computes the number of households receiving assistance and benefit levels (total and average per household) for each program by the following categories:

- housing type (renter, cooperative, owner)
- household size
- household type (with and without children, and pensioner type)
- household income groups (per capita or per household).

The model also compares changes in user-specified housing expenditures such as space rent, and utility prices to base period levels. The model was modified from its original form so that it could simulate many of the design issues raised in this report, including social program sequencing, formula modifications, changes in housing privatization rates, and changes in components of housing expenditures.

Measuring the Fiscal Impact of Rent and Utility Price Increases

We chose to simulate three scenarios using a variety of rent and utility assumptions. Our starting point is late 1994 since the HAIS model's data base standardizes all monetary variables at that time. For simplicity, all three simulations take place over a one-year period. For the first simulation (A), we held rent levels and utilities constant. Simulation A assumes *all* eligible households participate in the housing allowance program. For the second simulation (B) we increase rent and cooperative communal housing fees for households who live in cooperatives by 100 percent while maintaining utility prices at their 1994 levels. In addition, for households living in family houses the price of maintenance was increased by 50 percent to more realistically reflect an increased level of investment in owner-occupied housing. To more realistically portray program participation, the percent of eligible households expected to participate in the housing allowance program was set at 50 percent. In terms of the third simulation, C, we increase housing expenditures as in simulation B, raise the price of heating by 100 percent, and leave the participating rate at 50 percent.[3]

For all three scenarios, we chose not to alter the housing allowance formula from its traditional form. (That is, we did not subtract the subsistence minimum from gross income as proposed by some Ministry officials.) The MSR is based on average per square meter prices of rent and utilities using rate schedules for category I municipal housing. The MSR rates were computed for different household sizes and applied to all three types of housing tenure groups. The share of income devoted to housing cost ("r") was set at 20 percent, while the housing privatization rates (percentage of municipal and cooperative housing that changed became the property of the sitting tenant) for municipal and cooperative housing were set at 10 percent. By including utilities as part of the housing allowance we could simulate the impact of raising the price of heating since energy prices are currently subsidized for cooperative and rental households. Additionally, we set the HAIS model option for granting the minimum housing allowance benefit--the level at which benefits will not be payed--at Sk 50.

---

[3] These participation rates are more realistic than a 100 percent rate. We know of no housing assistance program in which all eligible household participate. Indeed, the participation rates in some Russia cities are close to 50 percent during the first few years of their housing allowance program. In Szolnok, Hungary the participation rate is about 42 percent, while in former East Germany it was about 50 percent after the second year.

Table 1.1
HAIS MODEL SIMULATION RESULTS FOR DECEMBER 1995
SLOVAKIA, 1994-1995

Tenure	Housing Cost Increase (Pct.)	Heating Increase (Pct.)	Particp. Rate (Pct.)	Number of HHlds ('000)	Total Allowance (Sk '000)	Average Allowance Sk/month	Housing Revenue Increase (Sk '000)	Utility Revenue Increase (Sk '000)
Senario A								
Renter	0	0	100	109	39,000	376	0	0
Coop	0	0	100	74	27,000	360	0	0
Family	0	0	100	240	65,000	270	0	0
Total:	n/a	n/a	100	424	132,000	311	0	0
Senario B								
Renter	100	0	50	97	68,000	744	128,000	0
Coop	100	0	50	70	49,000	701	76,000	0
Family	50	0	50	211	124,000	590	61,000	0
Total:	n/a	0	n/a	378	241,000	641	265,000	0
Senario C								
Renter	100	100	50	144	147,000	1,002	128,000	155,000
Coop	100	100	50	100	104,000	1,029	76,000	182,000
Family	50	100	50	308	285,000	914	61,000	48,000
Total:	n/a	100	n/a	552	536,000	964	265,000	370,000

Source: HAIS model, 1994 Microcensus

Table 1.1 shows the results of the three HAIS model simulations for December 1995. Under the conditions of scenario A, without any real increase in rent or utility prices, and 100 percent participation by eligible households about 25 percent of all households would receive a housing allowance benefit. Housing allowances would cost the government approximately Sk 132 million per month or about Sk 1.6 billion per year. The average monthly housing allowance would equal about Sk 311. Households living in family houses would receive the smallest benefit (Sk 270) while those living in rentals would receive, on average, the largest benefit (Sk 376).

Large rent and utility increases cause the cost of the program to rise. Scenario B and C assume a 50 participation rate for the housing allowance program and a 100 percent increase in housing prices (other than utilities except for heating prices in scenario C) for households living rental and cooperative units. Though the participation rate was cut in half compare to scenario A, the number of households receiving housing allowances under scenario B decreases by only 12 percent. Under the conditions of scenario B--with substantial housing price increases--only about 22 percent of all households in Slovakia would receive a housing allowance. But what is most interesting, is the fact that the increase in housing revenues from renters is almost twice as large as the benefits payed to renter household (Sk 128 million per month versus Sk 68 million per month in outlays). The overall increases in rent revenue over the base period level very closely matches the amount of subsidies attributed to rental housing conservatively estimated previously (Sk 1.5 billion per year additional rent revenue versus Sk 1.7 billion estimated operation and maintenance subsidy).

The results from simulation related to scenario C reveals the extent of additional revenue attributed to a 100 percent heating price increase. Indeed, about Sk 4.4 billion per year could be added to the coffers of heating companies through consumer-based subsidy while no household in Slovakia would have to pay more than 20 percent of its income toward housing expenditures. Under the current system, on-budget heating subsidies are payed directly to heating companies thereby providing little incentive to producers to provide energy more efficiently. With a consumer-base utility subsidy (coupled with individually metered housing units), heating prices could be increased to reflect the economic cost of providing this utility while protecting the poorer population from undue economic hardship.

These three simulations utilize the HAIS model to show that reducing housing and heating subsidies can lead to substantial fiscal gains for not only municipalities but also for the state budget through offsetting revenues. With a housing allowance rent and utility subsidies can be better targeted to those households who truly need assistance. The cost of providing heating can be more efficiently covered by direct payment from households who can afford to pay more for housing costs but need not pay more than a reasonable fraction of their total income. In this manner, the state can do away with heating subsidies through imposition of a well designed housing allowance. In addition, municipalities will benefit from additional revenues to increase their expenditures on the operation and maintenance of rental housing. Foremost, with a housing allowance lower-income household will be protected from undue economic hardship caused by housing cost increases.

SECTION II

INTEGRATING HOUSING ALLOWANCES AS PART OF SLOVAKIA'S SAFETY NET

Key Design Issues

As the government of Slovakia formulates plans to introduce a housing allowance it will need to address many issues related to its design and implementation. In this section we will focus on the issues related to formula design and the coordination of housing allowances with the other means-tested benefits aimed at sustaining the economic well-being of households. Some of these issues concern the *design* of the housing allowances, whereas others concern the program's *implementation*. The most important issues are:

How should the definition of income used in the housing allowance formula be coordinated with that used for other means-tested benefits?

How should the *"household*" (that is, the group of individuals whose income should be considered together) be defined for the housing allowance?

Which *reference period* should be used to measure income? How should How the reference period chosen for housing allowance be coordinated with that chosen for other means-tested benefits?

Should the benefit paid under other means-tested programs be included in the income used to determine the housing allowance benefit? Alternatively, should the housing allowance benefit be considered in determining eligibility and benefits for other programs? In other words, how should the different programs be "*sequenced*"?

Should the personal component of the subsistence minimum be included in the housing allowance formula? What are the consequences of its inclusion in terms of the amounts of housing allowance benefits received by households of different sizes?

An Overview of Slovakia's Safety Net

Social program benefits fall into three categories: social insurance, social support, and social assistance. This sub-section of the report provides a brief overview of these three systems to provide a context for program design. All three types of social programs are designed and implemented by the Ministry of Labor and Social Affairs.

Social Insurance. Social insurance is now separated from the state budget and financed by a system of compulsory contributions. It is intended to protect individuals against losses of income that are, at least in principle, insurable (i.e., due to retirement, loss of a job, illness, disability due to an accident or a chronic health condition.) The major types of benefits issued by the social insurance system are sickness benefits, unemployment benefits, and old-age, disability, and survivor pensions. These benefits can have a redistributive function, but redistribution is not their overriding goal.

Social insurance is the largest component of the overall system of social protection, since it provides benefits equal to about 20 percent of GNP, and has 1.4 million beneficiaries, representing about 25 percent of the population. However, because its benefits are generally not means-tested, it is also the component whose coordination with housing allowances poses very few problems. Therefore we will limit most of the subsequent discussion to the other two components.

Social Assistance. The system of *social assistance* is based on the principle that all citizens of Slovakia are entitled to a minimum level of income. The minimum level is established by the *Subsistence Minimum Law*, and is updated periodically to account for inflation and changes in per-capita income. Social assistance benefits are intended to support households who are "socially dependent", a criterion that is based essentially on having resources below the subsistence minimum. The basic form of intervention is a cash benefit equal to the difference between the income available to the family and the subsistence minimum. The income used for eligibility and benefit calculations is that observed in the preceding 12 months, and the family is subject to a verification of income every 6 months. The establishment of eligibility also requires the verification of assets owned by the family.

The presence of children is not a condition of eligibility for social assistance. In fact, in the first 4 months of 1995 about 90,000 households with children received social assistance, as well as about 90,000 households without children (whose members must be registered as unemployed.) Pensioners are not directly entitled to the basic social assistance benefit, because the minimum pension is already set at the level of the subsistence minimum. However, pensioners might be eligible for supplemental assistance in special cases, as are persons with disabilities. In cases of special needs (such as the need of a special diet) the subsistence minimum is raised by some pre-specified amounts. In addition to cash grants, the social assistance offices deliver other types of aid, including short-term loans and counseling. Total expenditures on social assistance amounted to about Sk 5 billion in 1995.

Social Support. The broad aim underlying the design of the system of *social support* is that it should comprise a range of benefits which will be available to people whose income might be above--in some cases substantially above--the subsistence minimum. Social support should be a means of assisting households with members not yet able to earn their living and those facing "special life events" with which they could not cope unaided. With few exceptions (such as birth and funeral grants), all benefits under the social support system are subject to a means-test.

The presence of dependent children is a condition that is usually needed for social support eligibility. In fact, *child allowances* --both "regular" and "supplemental"--are the type of social support that absorbs the largest share of resources and serves the largest group of beneficiaries. About 80 percent of households with children are currently eligible for child allowances. The projected budget for child allowances is over 10 billion Sk for 1996, about 60 percent of the overall social support budget. In terms of expenditures projected for 1996, in second position we find *parental allowances*, which are paid to parents who care for young children at home. Next are *transportation allowances*, which have only recently become available. All the remaining forms of social support (such as birth and funeral grants, student stipends, benefits for persons with serious handicaps) taken together represent less than the projected expenditure in 1997 on housing allowances of approximately Sk 2.6 billion.

Eligibility for child allowances is currently based on two income cutoffs, which are *multiples* of the subsistence minimum for the whole family. The subsistence minimum includes "unavoidable housing expenditures" or ZM(h). The amount of the allowance for each child is set as a *fraction* of the personal component of the subsistence minimum or ZM(p) pertaining to that child. The amount of the ZM(p) varies with the age of the child. If income is less than 150 percent of the subsistence minimum, the child allowance is set to 50 percent of the ZM(p) for each dependent child; if income is between 150 percent and 200 percent of the subsistence minimum, the child allowance is reduced to 30 percent of the ZM(p) for each dependent child. Households with incomes above 200 percent of the subsistence minimum are ineligible for child allowances.

Issues Concerning the Interaction of Housing Allowances with Other Means-Tested Benefits

Income used to determine eligibility. The draft Law on Social Support (Ministry of Labor and Social Affairs, November 1995) contains a very detailed list of items to be included in total income for eligibility determination. This list does not explicitly include income from assets--such as interest, dividends, and income from renting property. The fact that the taxation of interest and dividends is done through direct withholding, and that this income is not reported in the annual tax return can certainly pose some difficulties, but it does not seem reason enough to omit such sources from total income. The resources that should be considered in assessing the economic well-being of households do not necessarily coincide with what the tax system considers as taxable income (for example, in many countries pensions are not taxed but are considered as income in means-testing).

To establish eligibility for *social assistance,* the *value* of some assets is taken into account, which represents a stricter condition for eligibility. We believe that at least the actual income derived from these assets, such as the income from rental property, should be included as a component of total income used for social support eligibility determination.

Household definition. For child allowances, the natural group of individuals seems to be the *nuclear family*, since raising children is the direct responsibility of parents, and the fact that there might be other adults in the house can be disregarded. Such a definition seems appropriate for child allowances, but not for housing allowances. In the latter case the appropriate household definition, both to establish the MSR and to determine income, seems to be the group of all individuals *who are resident at an address.* This solution (the "all residents" solution) has two disadvantages: (1) it increases administrative costs, because in some cases the income verification put in place to determine child allowances is not sufficient; (2) with potentially more income recipients in the unit, the need for updating the benefit amount increases proportionally. Despite these minor disadvantages, we maintain that the household definition should include all residents living at an address.

Subtracting the personal component of the subsistence minimum. Staff at the Ministry of Labor and Social Affairs have contemplated a design modification to the standard formula for housing allowances involving the subtraction of the personal component of the Subsistence Minimum ZM(p). The formula would become:

$$HA = MSR - r * (Y - ZM(p))$$

Where ZM(p) is the sum of the personal components of the subsistence minimum. Their justification for this design alteration relies on a belief that if a certain amount of income is considered essential for survival, it cannot be considered available for paying housing expenses. It should be clear, however, that the inclusion of ZM(p) has important consequences for the way the program actually works. To better explore these consequences, it is useful to rewrite the above formula as:

$$HA = MSR - r * Y + [r * a * ZM(p)]$$

If a = 1, we have the proposed formula. If a = 0, we revert to the more standard formula. It is obvious that, once the distributions of MSR and Y are given, to keep expenditure within prespecified levels a=1 requires a larger value for r than a=0. Let us consider the two alternatives, which we label as:

"HA 1": a = 0, r lower

"HA 2": a = 1, r higher

These two alternatives have different consequences for the distribution of benefits across different types of households, since ZM(p) increases proportionally with family size, while presumably the MSR increases less than proportionally. For example, the MSR for a family of 6 is less than 3 times as large that of a family of 2, while the ZM(p) is roughly 3 times as large. With the "HA 2" solution, *large households will get a larger fraction of the total housing allowance expenditures* than in the case the HA 1 solution, if total expenditure is held constant in the two situations. There are two major consequences for including ZM(p) in the housing allowance formula. They are: (1) the inclusion of ZM(p) requires much larger values of "r"; and (2) it can generate a different distribution of benefits across different types of households. The HAIS model can be used to test the effects of subtracting out the personal component of the subsistance minimum from gross income in the housing allowance formula.

An explicit income cut-off for housing allowance eligibility. The proposed legislation for housing allowances *explicitly* mentions an income cut-off, expressed as a multiple of the subsistence minimum. However, such a cut-off is either redundant or inappropriate, since the standard formula for housing allowances contains an *implicit* income cut-off, equal to:

$$\text{cut-off for eligibility} = MSR/r$$

For incomes above this limit, benefits are zero, and the household is automatically ineligible. In practice, a minimum amount of benefits can be set (e.g., SK 40), to avoid paying very small amounts: everybody entitled to an amount between zero and the minimum could get the minimum (or nothing). The chosen value of r will imply a "phasing-out" of benefits at some multiple of the subsistence minimum, but where this happens can be predicted if good data on the distribution of income and household size are available. We believe that setting an explicit cut-off limit for eligibility could create unnecessary confusion.

Sequencing means-tested programs. When should benefits from one program be considered as income by another program, and in which order? This problem is not specific to housing allowances (or to Slovakia), rather it arises in every situation in which there are several means-tested programs for which some households might be eligible at a given point in time. This problem has been faced in the United States, where there are several means-tested programs (e.g., food stamps, housing subsidies, cash transfers to single-parent households with dependent children, social pensions).

One way to simplify the problem is to establish a sequence of programs that goes only in one direction: the benefits from one program are included in the income for the next program, *but not the other way around*. In other words, benefits from program A are considered as income for program B, but benefits from program B should *not be* considered as income for program A. If this rule is not followed, we could end up with a very complex benefit formula in which every program would depend on the parameters of every other program. When the "one-direction-only" rule is followed, there remains the problem of how to establish such direction, or sequence. There are no easy rules: it all depends on the purpose of each benefit, on the size of the population served, and by the administrative feasibility of the solution.

We believe that child allowances should come first since they are a universal benefit. The amount of the child allowance should be considered as income for subsequent benefits (in particular for social assistance and housing allowances), but the child allowance itself should be computed *without* taking the other benefits into account. It is less clear to us how the rest of the sequence should be completed. Should social assistance be computed first, including social assistance income in the housing allowance formula? Or should housing allowances be computed first, with social assistance playing a role only if income is still below the subsistence minimum?

Since housing allowances are considered part of the social support system, the advantages of an "housing allowance first" solution is that eligibility for all social support programs would be established first, leaving social assistance to be the program of last resort. This would help keep the two systems separate. This would also give social assistance a reduced role in terms of cash disbursement: if the maximum standard rent is large enough, it is possible that most households with children would be lifted above the subsistence minimum by the combination of child and housing allowances (as long as they apply for these programs.) This position of prominence for housing allowances would presumably increase the participation in this program, and also create less disincentives for work (or for underreporting incomes), because housing allowances "tax" earnings at a rate equal to “r” in the housing allowance formula, while social assistance because of its arbitrary thresholds taxes it at a rate of 100 percent.

Program sequencing has two types of consequences. First, what are the overall budget consequences of the alternative sequencing rules? Keeping all other parameters constant, does it cost more to have social assistance computed before or after housing allowances? Second. what are the distributive consequences of this choice? Do certain groups benefit more from one sequencing than from the other? By utilizing the HAIS model staff at the Ministry of Labor and Social Affairs can easily estimate the budget impact and distributional consequences of different sequencing strategies.

Reference period. The choice of the reference period is an issue in the implementation of means-tested programs in every country. The idea of giving help to those most in need *when* they need it, would imply that the reference period used to assess eligibility should be very recent and rather short, and that benefits should be continuously adjusted to reflect current economic conditions and need. However, such an ideal system is almost never used in practice, because of high administrative costs, and the burden imposed on the recipients.

Typically, income received over a certain period in the past is used as a proxy for income that presumably will be received for a certain period in the future. We will call the former the "reference period", and the latter the "prospective period". Some degree of discrepancy between reference period and prospective period will always exist. The real issues are how much discrepancy should be tolerated, and how to correct discrepancies when they arise.

Slovakia has two systems in place for means-testing, one for social support programs (mainly for child allowances) and one for social assistance. In the first system, the reference period for social support programs is the "last calendar year for which tax reporting is completed". This means that, from year t and year t+1, the income of calendar year t-1 is used to determine eligibility and benefits. The prospective period is therefore also one year, and runs from July to June. This system has the advantage of being able to use, as a basis for certification, the income reported in annual tax returns. This seems to be its major justification and strength. This system works well for those households in which income is relatively steady, particular when deriving from regular employment and pensions. The disadvantage of this system is that there is *on average a lag of 18 months* between when a benefit is paid and when the income (on the which the benefit is based) is actually received. So this system is not ideal for households with less stable income. The income received 18 months ago might bear little resemblance with that received today.

The system used for social assistance is quite different. Although we have conflicting information, the income used for eligibility and benefit calculations appears to be that which is received in the preceding 12 months, with more importance given to the income received in the most recent months, if that gives a better indication of current condition. The family is subject to a verification of income every 6 months. Changes in circumstances that can lead to a change in benefits must be reported to the office within 8 days.

Given the attempt to integrate housing allowances into the system of social support, we understand that the preference would be to extend the "tax year system" to housing allowances. However, we believe that this system has limited effectiveness *in terms of its ability to help those in need when they need it*. Moreover, the savings in terms of administrative costs from extending this system to housing allowances depends to a large extent on the degree to which the population entitled to housing allowances will coincide with that receiving child allowances. This overlap might be rather limited, because households without children will be eligible. A system of income certification that works relatively well for the majority of child allowance recipients (especially those who have relatively steady incomes) might not be appropriate for a population that is more disadvantaged and might experience wider income fluctuations.

The role of the subsistence minimum. As the preceding discussion suggests, both systems of social assistance and social support rely heavily on the subsistence minimum as a key parameter to determine both eligibility and benefits (while the social insurance system relies on it only to determine the minimum pension.) We believe such a central role of a subsistence minimum is more justifiable for social assistance than for social support. Since social assistance is designed to guarantee a minimum standard of living, a direct measure of such a minimum is essential.

However, the rationale for using the subsistence minimum as a key parameter for the system of social support is less clear. While guaranteeing 100 percent of the minimum to all households is a clear and intuitive notion, there is nothing particularly compelling about paying 30 percent of child support costs if the family income is more than 150 percent of the subsistence minimum. In this case, the use of the subsistence minimum parameter seems to be largely a matter of convenience, and many other conventional quantities could be used to set the income limits. For example, an income limit could be based on a given percentage of median income, adjusted for family size. Fifty percent of median income is used in many countries as a conventional measure of determining eligibility for programs.

A major advantage of using the subsistence minimum as a key parameter is that, by updating it for inflation, all the income cutoffs and the amounts of benefits are automatically updated. However, we believe that the use of a quantity that has a strong connotation of a "minimum" has also many disadvantages. Any attempt to increase such minimum in *real* terms to make it really adequate for survival, would have a "ripple effect" throughout the entire system, affecting millions of recipients and the entire state budget. Conversely, needed revisions of such minimum might be held back for fear of altering the overall state budget.

We believe that some consideration should be given to having *two distinct parameters*: the Subsistence Minimum, which is applied only to social assistance (and to minimum pensions), and another "social standard", perhaps linked to the median family income, which is used for eligibility for social support.

SECTION III

DETERMINING THE MSR IN THE HOUSING ALLOWANCE FORMULA

Background

The maximum standard rent (MSR) setting in the formula will affect which households are eligible for the program, the amount of assistance those households receive, and the total outlays of the housing allowance program. Key considerations in establishing the MSR include:

- The MSR is based on appropriate standards.

- Adjustments can be made as necessary without extensive and costly analyses.

- Incentives are maintained to encourage appropriate levels of housing consumption.

The proposed formula-based housing allowance provides incentives for households to consume housing closer to the MSR. For example, lower income households that are over consuming (i.e., occupying housing larger than provided for in the MSR) would have a financial incentive to seek less expensive housing in order to pay less of their income for housing. Larger households that are under consuming housing could, with a housing allowance based upon the MSR, better afford larger dwelling units. The housing allowance facilitates the economic incentives to move to housing more appropriate in size for the household's needs. Moreover, housing allowances would provide households the freedom to “shop” for housing that suits their needs in terms of size, cost, quality, and location.

Each variable in the housing allowance formula affects who is eligible and how much they will receive. Two of the three basic parameters appear to be established for the initial implementation of the program. A definition of income (Y) for the housing allowance program has been proposed that is quite similar to the definition currently used to determine other social support benefits. In addition, the maximum share of income devoted to housing costs ("r" in the formula) has been set at 20 percent based on the HAIS model simulations. Therefore, the principal remaining element of the formula to be determined is the value of the MSR. The MSR is an approximation of typical housing expenditures for a unit that is big enough for a given household size.

Theoretical Considerations for Determining the MSR

It is important that the standard not be too low since this might force many eligible households to pay more than the established "r". A more appropriate standard would be based on the average expenditures of typical existing units or perhaps some fraction of the average expenditures. Some housing allowance programs restrict eligibility to households for whom the formula yields an amount above a certain minimum. The theory is that amounts below this level are so low that the benefits to the household are too low to justify the administrative costs of making benefit payments.

The basis for establishing the equivalent of the MSR in many Western countries is to conduct surveys of actual market prices for standard units and determine an expenditure standard for a unit that is appropriate for each size and type of household. Rent setting may be formula driven or may require legislative or administrative approval. The latter may involve considerations such as overall budget limitations in addition to increasing housing costs. For example, the U.S. equivalent of MSR (known as the FMR or Fair Market Rent) was established for its housing allowance for many years at the 45th percentile of rents (including utility costs). The actual FMRs are updated each year based upon survey data on current housing expenditures for each major metropolitan area and rural counties.

For Eastern European countries, in which market conditions for housing and housing services are not well established, the MSR might be set as a standard rate for a household of a particular size. This is calculated by multiplying a standard or average amount of living space or total space (expressed in square meters) by per square meter prices for housing, services, and utilities. In some cases, utility expenditures are calculated on the basis of number of household members rather than square meters. The MSR is typically expressed as a monthly rate that varies by household size.[4]

The criteria for establishing the MSR can be very complex or quite simple. Generally, we recommend using a simple method that is based on the best single standard (varying only by household size) for a basic or most typical housing. It is the basis for determining the amount of social assistance for housing that should apply to all households of the same size and income, regardless of their actual housing consumption. The differences in their actual consumption are reflected in the actual housing expenditures for their units, not the MSR.

Setting the Social Housing Norm

The MSR can be established in a very complicated way that takes into account housing type (family housing, municipal housing, and cooperatives), location, or even by the types of fuel used in the unit. However, we believe that this complication is not necessary to the design of an effective and equitable program. Instead, we recommend a single standard that applies to all households.

---

[4] In some programs, two-person households are separated into those containing two adults and those made up of an adult and a child. Typically, the households with two adults have the same MSR (or at least are based upon the same square meter standard) as a single person household, while the household with an adult and a minor would be assigned a larger MSR based upon a larger number of square meters.

One approach would be to use municipal housing as the basis for developing the social norm. Over the past several years, the majority of the housing built and allocated has been municipal or cooperative housing. If municipal housing standards are used as the basis for setting the MSR, we recommend the standard be based on Category I housing. This is the highest standard (with full amenities) and represents just over 80 percent of all public and cooperative housing. Family housing varies greatly in terms of size, age, design, and quality, and it would be very difficult to establish a separate national standard for such housing.[5]

A recent study of housing expenditures conducted by the research institute of the Ministry of Labor and Family Affairs, found that average overall housing costs do not vary greatly by tenure type (See Table 3.1). The expenditures for each of three tenure groups in Slovakia vary by their components, but the variation in the total expenditures is not large. This makes it easier to adopt a single standard; but, even if there was greater expenditure variation across these tenure groups, we would recommend that consideration be given to a single standard for housing consumption based upon the expenditures for typical municipal housing differentiated by size.

As the housing market develops, prices will vary more by location. However, standard municipal housing units are currently about the same size with little expenditure variation throughout the country. Therefore, there presently is no basis for establishing a standard that varies by area, though such a differentiation may need to be reflected in the MSR in the future.

[5] There are three types of tenure forms in Slovakia. Family housing refers to owner-occupied housing, concentrated in rural areas and usually built through the self-help method. While cooperative housing is a form of ownership but highly subsidized by the state with a discounted loan. Municipal housing is former state housing that was devolved to municipalities in 1991 and represents the bulk of rental housing.

TABLE 3.1
AVERAGE HOUSING COSTS
SLOVAKIA, 1992

	Slovak Crowns per Month per Household			Percent of Total		
	Rental	**Coops**	**Family Houses**	**Rental**	**Coops**	**Family Houses**
Cost Category						
Net Rent	319	332	n/a	29	28	n/a
Flat/House Maintenance	35	42	153	3	4	15
Water & Sewer	68	75	19	6	6	2
Municipal Utilities	50	47	15	5	4	1
Energy Costs	646	698	839	58	58	81
Total Housing Costs	1118	1194	1041	100	100	100
Components of Energy Costs						
Central heating & hot wat	423	506	2	66	73	0
Electricity	136	136	248	21	20	30
Gas	41	41	50	6	6	6
Solid fuels	46	12	539	7	2	64
Total Energy Costs	646	698	839	100	100	100

Source: Adapted from Table 3, page 30 of "Social Policy in Housing: Problems, Their Management and Issues" by Danekova and Rihakova, Research Institute of the Ministry of Labor and Social Affairs Bratislava, Slovakia.

TABLE 3.2
HOUSING UNIT SIZE IN SQUARE METERS
HISTORICAL STANDARDS AND CURRENT CONSUMPTION BY HOUSEHOLD SIZE
SLOVAKIA, 1992

Household Size	Living Space		Minimum Standard		Total Space	-
	Assignment Standard	Construction Standard	Living	Total	Actual Average	Actual Median
1	18	36	12.5	23.5	44	40
2	30	48	21.0	28.5	59	58
3	42	65	32.0	37.5	64	64
4	54	75	36.4	48.5	67	67
5	66	84	n/a	n/a	70	68
6+	78	94	n/a	n/a	68	69

* Municipal Housing Only.

Optional Approaches to Establishing Housing Norms

There are several approaches to establishing a social norm for housing consumption. It could be expressed as the current construction norm, a housing waiting list eligibility norm, or a typical amount based upon the existing housing. These standards or measures are typically expressed in square meters of living space or total space.

Another alternative is to base the standard on a number of rooms in the unit for each family size. Using the number of rooms is a very convenient way of expressing the standard, but it is important to consider whether this will be meaningful to eligible households since housing size in Slovakia has always been expressed in terms of square meters of space.

Historical and current standards are available to illustrate these alternatives. This is not an exhaustive list and it is not clear as to the extent to which these standards actually affected housing construction or assignment. Table 3.2 illustrates an historical assignment standard, a new construction standard from the 1980s, and a historical minimum occupancy standard. In addition, this table provides data on actual mean and median floor space consumption for municipal renters, based upon the Slovak Microcensus.[6]

There is considerable variation between the historical standards, particularly as compared to actual consumption. It appears that the greatest variation is in the one-person households. This should be expected because many of these households reside in larger units than would normally be assigned to small households, but there are none in smaller than anticipated units because this group is expected to have the smallest dwellings. For larger households there is some tradeoff between those overconsuming and those underconsuming housing space resulting in an average that is closer to the assignment and construction norms and from the actual current consumption.

Table 3.3 compares the median total space by type of housing by the number of persons in the household. This table shows that family housing is significantly larger in terms of square meters, with cooperatives generally slightly larger than municipal units. For renter units, there are small increases in floor space for each additional household member.

[6] The Microcensus is survey that is conducted throughout Slovakia of randomly selected households every other year. This file can then be “weighted” to represent the entire number of estimated households. This data file contains detailed information on housing and household characteristics.

TABLE 3.3
UNIT SIZES BY HOUSEHOLD SIZE AND TENURE
SLOVAKIA, 1992

Number of Persons in Household	Median Square Meters of Total Space By Type of Housing		
	Municipal Housing	Cooperative Housing	Family Housing
1	40	45	64
2	58	62	76
3	64	67	87
4	67	69	96
5	68	70	99
6+	69	69	97

Source: MicroCensus 1992.

Housing Components Included in the MSR

Another consideration in determining the MSR is which components of housing expenditures to include. The Slovak proposal is that all housing expenditures be included (except telephone). Basing the standard on municipal flats would including using net rent, maintenance fees, water and sewer charges, municipal utilities, and fuel expenditures. However, it is possible to design the MSR to exclude one or more of these expenses. For example, the Germans exclude heating expenditures from their calculation of the subsidy in order to encourage conservation. For Slovakia, where few units are able to be metered for heating, we recommend using *all housing costs* as the basis for MSR.

Rates to Apply to the Social Norm for Space

Once the social norm is established, then the current rates for the various components of housing services can be multiplied by those space norms to calculate the MSR. If the charges are expressed in terms of number of persons, then this can be built into the formula. If the MSR is based on a number of rooms, then some measure of expenditures based on the typical size for each room category will be needed in order to calculate expenditures by room category. The key is to establish the *expenditures of the most typical situation* and not take into consideration (at least initially) inequities that may occur because households have, for example, different housing types or sources of fuel.

Use of the Housing Portion of the Subsistence Minimum

One option being discussed for the MSR is to use the “unavoidable housing cost” component of the subsistence minimum (ZM(h)) used by the Ministry of Labor and Social Affairs for determining eligibility and benefits in other programs. One important advantage of using this component as the MSR is that it has some credibility due to its use over time to establish benefit levels for other programs. However, since the subsistence minimum is legislated it would be cumbersome to update this rate and its extensive use for determining other benefits, as discussed in the previous section, may be a potential disadvantage.

Having all social benefits tied to a subsistence minimum may complicate program delivery. For example, policy makers may determine that a change in the subsistence minimum affects so many program outlays that an increase could have an inflationary effect that erodes the buying power of the increase, and hastens the need for another increase. Fear of inflation and higher outlays might delay updates to the subsistence minimum. In addition, using a single measure to adjust the benefit level in several key programs may restrict policy makers’ flexibility in controlling costs and achieving the best balance between costs and household needs.

SECTION IV

PROGRAM IMPLEMENTATION OBJECTIVES

Background

There are several goals in designing an effective housing allowance program. The goals relates the two criteria used to evaluate program design--equity and efficiency. For example, we want the program to treat equally all households in similar circumstances. We want the assistance payment to reflect as closely as possible the actual income of the household at the time the household is making its housing payments. We want to minimize errors in payments (and certainly the opportunity for fraud), but we also want to minimize administrative costs. When these goals compete, the design challenge is to balance these objectives to achieve the purpose of the program.

Key Design Features Related to Implementation

This section of the report reviews selected aspects of the administrative structure of the allowance program and its implementation. For each, we discuss some alternatives, and then make a recommendation for the program.

Public information and outreach. How well the program is communicated to potential applicants and the general public can have a major impact both on administrative costs and public acceptance of the program. Too often, this outreach function is underestimated and programs spend considerable resources to clear up misconceptions, which sometimes threaten public support for the program.[7]

[7] This is especially true in Eastern Europe since first year participation rates for most programs have been rather low. See Annex A for a description of programs and household response to a new type of housing assistance.

A high quality public information campaign can be very important in controlling administrative costs. If officials can effectively communicate who is eligible and how a household can determine if it is eligible, the time spent answering questions and processing ineligible households can be reduced. It is worth some investment to avoid processing ineligible households, not only because of the wasted time and resources but also to avoid the frustration and ill will that may result when households make the effort to attend an interview, only to be told they are ineligible.

There are obvious benefits in having an informed general public. There will be critics of most public policy, especially if it relates to housing, but at least the opposition should be based upon the actual facts related to the program, not on some misunderstanding of program requirements. Also, a well informed public can better evaluate the program and any criticisms that are made of the program. The public information campaign can also help establish reasonable expectations about the duration of benefits, the effort required to participate, and the amount of assistance households will receive.

We recommend assigning responsibility for information and outreach to a person or office. The promotional campaign should include public announcements that are carried by the media. This outreach effort should be supported locally through the Ministry's District Offices and other government and private offices. Local offices should be prepared to provide staff for meetings of local groups to explain the program.

Taking applications. Many housing allowance programs use a two or three-step process for enrolling households into the program. Some require a preliminary application that is used to screen out those obviously ineligible for the program, and place those who appear to be eligible on a waiting list. Some programs with long waiting lists may require that households update, or provide more thorough information than was provided in their preliminary application, when they get near the top of the waiting list. Preliminary application processing is followed by the enrollment interview, or alternatively, a review of a written application in which questions are asked about items that are incomplete or unclear.

For example, one approach to processing applications is to publish the basic features of the program and perhaps even a worksheet that households can use to estimate their eligibility. Households that believe they are eligible and wish to participate would be encouraged to call their District Office to schedule an enrollment interview. Applicants should be told during the scheduling call what documents and other information they need to bring to the interview, and written confirmation of the time and place and the information they are to bring should be mailed to them. However, time and expenditures for such mailings may make written confirmations infeasible.

We recommend a streamlined application procedure for the Slovak program. It appears likely that large numbers of households will be eligible on the first day of the program. This will provide considerable pressure for rapid processing. Consideration should be given to providing written materials in newspapers at District Offices and at other locations to explain the program to potential applicants, and to providing a worksheet to enable households to estimate whether they are eligible. Those who wish to apply would be encouraged to telephone their District Office to schedule an interview. This approach is designed to minimize the number of ineligibles who apply while requiring the fewest number of steps to enroll in the program. It should help enable District Offices to process large numbers of cases in a short time.

Processing enrollments. Experience with housing allowances and other means-tested programs in other countries confirms the value of a face-to-face interview. Such interviews help ensure that the household has correctly and completely reported the required information and that the household understands the program, and their obligations and rights under the program.

To ensure a consistent presentation about how the program works and to more efficiently impart this information, many programs conduct group briefings for households. Often these use slide and sound or video tape presentations. Typically, one or two staff persons present the prepared materials and answer questions after the presentation.

An alternative is to have the household submit a detailed application form and only have staff review it to be sure that it is complete and appears to be consistent. This has the advantage of requiring less staff time, but it is less likely to be accurate and provides more opportunities for misreporting by applicants. It is also likely to be less effective in reinforcing the importance of accurate and complete reporting and other program obligations.

Administrators can speed processing if they have access to key information. For example, if administrators have access to computer files containing up-to-date information on all or most of the income sources of a household (e.g., pensions, child allowances, unemployment compensation, last year's taxable income), there is less need for probing so the interview can be shorter by focusing only on those elements that cannot be confirmed by computer. In any case, we recommend a face-to-face interview to reduce misreporting and help ensure communication of clear expectations for participants and of the consequences of noncompliance.

Verifying income. While the measurement of income cannot always be exactly accurate, there can be an expectation of accurate implementation of verification procedures. Experience from other countries suggest that:

- The rules for measuring income must be written and they must include clear decision rules for estimating each type of income.

- There should be a set of forms with written instructions that ensure that all questions are asked and answered in each interview.

- There should be an expectation that no exceptions will be granted. If the rules do not appear to fit the circumstances at hand, change the rules nationwide so that all such cases can be treated equally.

- There should be a requirement that all sources that cannot be confirmed by computer must be documented by a responsible third party whenever possible.

- There should be adequate training for staff on how to apply the written guidance.

- There should be a system for regular meetings, perhaps by telephone, during which representatives of District Offices can raise questions or make suggestions regarding documents and procedures.

- There should be a system of internal quality control reviews at the District Office level, and an additional review of all District Offices by the Headquarters Office to ensure that the program is being implemented consistently throughout the country.

We recommend that Slovak officials adopt a system of prospective measurement of income, which gives great weight to current income information, and is the approach they are currently using for child allowances and social assistance. To simplify verification, we also recommend that *detailed guidance be provided to staff on how they are to consistently treat all regular and irregular sources of income*, including part-year income. We further recommend rules that minimize the need for interim recertification of income.

Treatment of assets and income from assets. Some housing allowance programs measure the value of assets held by the household and deny participation when asset values exceed a specified limit. Some programs deny participation to households who possess certain types of assets (e.g., the City of Moscow denies participation to any household that has control of more than one residence). Other programs focus on counting income or imputed income from assets.

In valuing assets, some programs count personal property (e.g., automobiles, jewelry, furniture) as well as real estate, savings, and cash on hand. In others, personal property is not counted. Some exclude business assets because those are required to produce the business income that is counted. Some programs ignore the value of the assets and only count the actual income received from assets. Others attempt to convert all assets to an income stream by determining an estimated current value for each asset and then taking the actual income if income is produced and imputing income for those assets that do not produce income.

Administratively it will be easier for Slovak officials not to attempt to impute income for non-income producing assets. It appears that this would be consistent with rules for other assistance programs now in place. However, over time it is likely that issues of public fairness will be raised when cases are identified where households have extensive land holdings that are not producing income or producing very little income compared to the value of the asset itself. While it may not be feasible to adequately value assets to impute income to them at the present time, it may be useful for the housing allowance program to ask questions from the beginning about household assets to better understand the implications of this method and to begin considering how these assets might be treated in the future.

Regular recertification of eligibility and benefits. There is a wide range of options in determining how frequently household circumstances are reviewed and benefits recalculated. Most programs reexamine income and household circumstances annually, typically counting any benefits in effect on the anniversary month of the household's initial enrollment. However, there are other alternatives depending upon the size and frequency of changes in household circumstances, the frequency of changes in housing expenditures that might affect the amount of the assistance payments, and the administrative resources available.

Slovakia's inflation rate has been stable for some time and lower than that of many of the countries in Eastern Europe that are now implementing, or considering implementing housing allowance programs. We therefore recommend that recertification be conducted annually. However, if wages, other sources of income, or prices of housing and related services change a lot, consideration should be given to modifying the benefits more frequently.

Special or interim recertifications as changes occur. Some programs require households to report some changes when they occur rather than wait until the next regular recertification. For example, households might be required to report all changes in household composition or any situation in which a previously unemployed person becomes employed. Some programs require that all increases in income must be reported. Others require increases above a specified threshold to be reported (decreases below a similar threshold may also be reported). In all these cases, the housing allowance office conducts a recertification and adjusts benefits accordingly. Some programs only examine the element of program eligibility where a change is reported, but require that if a loss of income is reported then the household must also report any increases in income.

We recommend that Slovakia implement a policy that requires households to report when household composition changes (to avoid providing assistance for the same person in two different households), when unemployed persons become employed (because of the large amount of income this normally implies), and when other changes occur that increase income above a specified level. Households should be able to report losses of income beyond a similar level. In general, however, it is best to keep the list of changes that must be reported as they occur to a minimum. The more things households are required to report, the less clear they will be about whether they are required to report certain changes. As a result, they may begin reporting changes they are not required to report. But even worse is a failure to report when it is required. This may result in a hardship for the household as they receive lower future benefits while they repay the overpayment, and it will be a significant administrative workload for the housing allowance office to set up and monitor the deductions from future benefits.

Monitoring and quality control. There are many opportunities for error in means-tested programs. For example, there are reporting errors by participants, reporting errors by third parties, misapplication of program rules, failure to report changes as required, and failure to process cases in the time required. There is the potential for intentional and unintentional errors both on the part of the participants and the staff. To maintain an equitable program and to retain public support, these errors must be minimized. There are many aspects of error control that can be built into the system through good forms and procedures, computer edits, and simplified procedures. But, in addition, there should be a program of quality control reviews of all aspects of the program. Every transaction should have some probability of being selected for a detailed review by a different staff member.

We recommend development of a formal quality control review procedure that would be implemented by staff at each District Office. In the very early days of the program, all cases should be reviewed by a supervisor or quality control specialist to ensure accuracy and consistency. As experience indicates that staff are applying the rules properly, the sample for review can be reduced accordingly to the point where eventually about 10 percent of all transactions should be reviewed. We also recommend that the Ministry be staffed to conduct management reviews of the District Offices to ensure consistent program operation and to identify problems as early as possible. The reviews should determine if all required functions (including quality control) are being performed and they should include a review of a significant random sample of transactions.

Sanctions for program participants. It is very important that there are clear sanctions for households that fail to comply with program rules. This should at a minimum include repayment of any amounts received due to errors in reporting made by the household.

In cases where the agency is able to demonstrate that the household purposefully misreported to obtain benefits to which they were not entitled, there should be additional sanctions. For example, in some programs these households have their participation terminated forever or for some specified period of time. Whatever the choice, the *sanctions should be meaningful and consistently applied in order to reinforce to households that they must accurately report as required by the program.*

Key Elements of Program Implementation

Too often inadequate attention is paid to actually implementing a new program once it is designed. Even the best designed program is unlikely to operate effectively unless adequate planning is made for implementation. This section discusses some key aspects of program implementation and makes some recommendations for the Slovak program.

Ministry officials have proposed a plan of using 1996 to prepare for implementation in 1997. During 1996, the legislation would be completed, regulations developed, systems (e.g., computer systems, forms and procedures) developed and installed, and an initial staff recruited and trained as trainers. The larger staff would be assigned and trained in the final weeks of 1996. This seems to be a prudent approach , *but considerable work is required to meet this schedule.*

One of the most important tasks will be to develop an overall plan for the implementation of the program. The plan would include a comprehensive schedule that would identify the major tasks and milestones. It is important to identify which tasks must be accomplished prior to others, and to identify the resources that will be required to implement and operate the program.

As Slovak officials begin this planning, we offer several suggestions for their consideration.

- # *Leadership*. A critical element of success in the implementation and administration of the program will be the provision of competent program leadership.

- # *Adequate Funding.* There must be sufficient funding for not only program benefits, but also for a skilled administrative staff, and the office space and other support systems they need to do their jobs.

- # *Written Program Guidance*. Clear and comprehensive written program guidance should be readily available for use by program administrators and workers.

- # *Insure Timely Updates to Written Guidance*. Rules have to be updated and clarified for all on a timely basis.

- # *Training.* If the program is to be implemented consistently throughout the country and staff are to be held accountable for following the program rules, a well designed training program is needed.

- # *Program Forms for Collecting Information*. Considerable attention should be given to developing well designed program forms to be used to solicit information required from households and other parties.

- # *Program Software*. As soon as the basic program design is determined, work should begin to develop the software needed to support the program.

- # *Reporting and Quality Control System*. A reporting and quality control system should be designed and implemented from the very beginning of the program.

- # *Internal Controls*. To ensure program integrity, the program should be designed with adequate internal controls that separate eligibility decisions from the actual payment process.

Adequate Sanctions for Staff. It is very important that program managers have the power to take action when program abuse occurs, either against participants or staff.

- # *Transmitting Program Funds*. There must be a mechanism for transferring the funding required for subsidies and administrative costs on a timely basis. However, there should be clear separation of assistance and administrative funds.

- # *Incentives for Managers*. Special care should be given to the design of incentives for administrators. Simply saving administrative costs should not be the basis for bonuses for managers.

Many of these activities must take place simultaneously and this will present a significant control problem. When all or most of the key design decisions are in place, work should begin on the development of the basic program forms (e.g., enrollment application, recertification, documentation and verification) and the Procedures Manual. As the details of processing are worked out in the development of the Procedures Manual, work should begin in developing the software to support the program. Once the program is essentially designed and the workload is reasonably clear, then work should begin on establishing job requirements and descriptions, and determining office space and office equipment requirements. A plan should be developed for having these offices ready to go by the time the program opens.

REFERENCES

Bundesministerium fur Raumordnung, Bauwesen und Stadtebau, 1993. *Wohngeld und Mietenbericht,1993*, Bonn, Germany

Bzdúch, 1995. *Rent in Relation to Costs in the Former Subsidy System and Today's Municipal Apartments,* UEOS, Institute of Economics and Housing Construction, Bratislava, Slovakia.

Conway, Francis J., 1995. Memorandum, *Update on Local Finance in the Slovak Republic, 1994-1995.* The Urban Institute, Washington, D.C.

Daneková, P. and R. Rihaková, 1995. *Social Policy in Housing: Problems, Their Management, and Issues.* Research Institute for the Ministry of Labor and Social Affairs, Bratislava, Slovakia.

Howenstine, Jay E., 1986. *Housing Vouchers - A Comparative International Analysis.* Rutgers University, New Brunswick, New Jersey.

Ivani…ka, Koloman, 1995. *Development of Housing Markets in Slovakia, Problems and Proposals for the Future,* Paper presented at the First International Real Estate Society Conference, Stockholm, Sweden, June.

Kepkova, Michael and Jiri Dlouhy, 1995. *State Social Support,* Publisher Unknown, Prague, The Czech Republic.

Kingsley, G. Thomas and Priscilla Schlegel, 1979. *Analyzing Allowance Program Administrative Costs: Account Structures and Methodology,* Rand Corporation, Washington, D.C.

Mark, Katie, and I. Tosics, and S. Erdosi, 1995. *Means Tested Housing Allowances in Hungary: Evaluation of the Szolnok Program,* Metropolitan Research and the Urban Institute, Budapest, Hungary.

Martini, Alberto, 1995. Memorandum, *Integrating Housing Allowances in the System of Social Support and Social Assistance of the Slovakia: A Preliminary Look at the Issues,* The Urban Institute, Washington, D.C. July.

Mayo, Stephen K., 1986. *Sources of Inefficiency in Subsidized Housing: A Comparison of the U.S. and German Experience,* Journal of Urban Economics, Vol. 20, p.229-249.

Mi±elsons, M~ris, 1993. *Housing Allowances: Assessing the Potential for Slovakia*, The Urban Institute, Washington, D.C. December.

____________**.** 1996. Memorandum, *Moving Towards Full Cost in the Rental Housing, Slovakia*, The Urban Institute, Washington, D.C.

Ministry of Construction, 1995. *Analysis of Housing Management with Special Regard to the Use of Revenues from Rent for Administration, Repairs, and Maintenance of Housing,* Republic of Slovakia, Bratislava, Slovakia.

___________**.** 1995. *Conception of the State Housing Policy by the Year 2000,* Republic of Slovakia, Bratislava, Slovakia.

Ministry of Labor and Social Affairs, 1994. *The Ten Commandments to Contribution to Rent*, Prague, The Czech Republic, January.

Ministry of Labor and Social Affairs, 1994. *Principal No. 4, Income and Income Testing,* Republic of Slovakia, Bratislava, Slovakia.

Rizor, Eugene, and M~ris Mi±elsons, 1995. Memorandum, *Determining the Maximum Standard Rent In the Housing Allowance Formula,* The Urban Institute, Washington, D.C.

___________**.** 1996. Memorandum, *Implementation Issues for the Housing Allowance Program in Slovakia,* The Urban Institute, Washington, D.C.

Struyk, Raymond J., Alexander S. Puzanov, and Lisa A. Lee, 1996. *Monitoring Russia's Experience with Housing Allowances,* The Urban Institute, Moscow, Russia, March.

Struyk, Raymond, Jennifer Daniel, Charles Hanson, Nadezhda Kosereva, and M~ris Mi±elsons, 1993. *Implementing Housing Allowances in Russia: Rationalizing the Rental Sector,* The Urban Institute Press, Washington, D.C.

Vaughan, Roger, 1995. *A History and Overview of Ukraine's Housing Subsidy Program,* PADCO, Keiv,Ukraine, November.

ANNEX A

OTHER COUNTRY EXPERIENCE WITH A CONSUMER-BASED HOUSING SUBSIDY

Background

The concept of a means-tested consumer-based housing subsidy is not unique to Eastern Europe. The first use of a consumer-based housing subsidy dates back to the early 1900s in Europe. Many countries in Latin America have offered grants to poor households for the purchase of new private sector housing. The United States' Department of Housing and Urban development has promoted the use of housing allowances for low-income renters. Today, means-tested consumer-based housing subsidies are increasingly used throughout the world because they have proven to be a relatively efficient and equitable way of providing housing subsidies.

The design of the subsidy can vary a great deal among countries. For example, central and local governments may combine resources to fund a subsidy program or they may separately administer programs. In all the countries, eligibility is determined by means-testing households using either their current income or a combination of income and assets. In some countries the subsidy does not vary in direct proportion with need nor is it available to all tenure groups. Finally, in some countries, the consumer-based subsidy is combined with other forms of housing subsidies such as housing production programs. Table A1 shows the countries that currently administer a means-tested consumer-based housing subsidy.[8]

[8] This table shows only those countries that use a direct consumer based subsidy. By definition, this type of subsidy is payed directly to the household or in some cases to a landlord where the subsidy recipient resides. It is in contrast to production-based subsidies that are linked to the housing unit. We show countries that have documented their experience with a consumer-based housing subsidy.

Table A1
CONSUMER-BASED HOUSING SUBSIDY PROGRAMS BY COUNTRY

	Type of Subsidy	Tenure	Date	Source of Funding
Ongoing Programs		O-owner R-renter		N-national L-local
Latin America				
Chile	capital grant	O	1978-present	N
Costa Rica	capital grant	O	1986-present	N
Colombia	capital grant	O	1991-present	N
Uraguay	capital grant	O	1991-present	N
El Salvador	capital grant	O	1991-present	N
Paraguay	capital grant	O	1991-present	N
Western Europe				
Germany	allowance	O/R	1955-present	N/L
Sweden	allowance	R	1930-present	N/L
U.K.	allowance	R	1970-present	L
Netherlands	allowance	R	1970-present	N/L
France	allowance	R	1948-present	N/L
Austria	allowance	R	1960-present	N/L
Switzerland	allowance	R	1950-present	L
Norway	allowance	O/R	1960-present	N/L
Findland	allowance	O/R	1941-present	N
Denmark	allowance	R	1955-present	N
Eastern Europe				
Poland	allowance	R	1995-present	N
Czech Republic	allowance	O/R	1993-present	N
Slovakia	allowance	O/R	expected 1997	N
Hungary	allowance	R	1994-present	L
Estonia	allowance	R	1994-present	N
Latvia	allowance	R	1994-1995	N/L
Lithuania	allowance	R	1994-present	N
Ukraine	allowance	O/R	1995-present	N
Belarus	allowance	n/a	n/a	N
Russian Cities	allowance	R	1992-present	L
Australia	allowance	R	1945-present	N
Canada	allowance	R	1970-present	L
South Africa	capital grant	O	1996-present	N
United States	voucher/certificate	R	1979-present	N

Source: Howenstine, 1986; Ferguson, Rubinstein, and Dominguez, 1995;
South African Ministry of Housing, 1995; World Bank, 1985, The Urban Institute 1993-1996

n/a - not available

Regional Experience with Consumer-Based Subsidies

Latin America. Housing assistance in Latin America has evolved along with the broader process of economic reform sweeping this region. Starting with Chile in the early 1980s, many Latin American governments have begun to redefine their role from a direct provider of housing to an enabler of the private sector housing market. Housing subsidy initiatives in Colombia, Costa Rica, El Salvador, Paraguay, and Uruguay follow the "Chilean model".

The Chilean model involves three basic policies that: (1) discontinue direct government production of housing and shift that function to the private sector, (2) provide one-time government capital subsidies to households for the purchase of housing and limit other indirect or implicit government housing subsidies, and (3) institute transparent systems of selecting households that will benefit from government housing subsidies based on current income and a savings contribution. The Latin American programs use rationed (i.e., they are not an entitlement) resources from the central budget and are directed to needy households who do not own a house.

Western Europe.[9] Governments in this region of the world have effectively operated housing allowances for several decades with a wide variety of strategies. Most Western European countries introduced allowances following World War II. The Dutch were the first Western European country to introduce a housing allowance to renter households. In 1930, Sweden introduced an allowance for households with children with the intent of increasing the supply of housing for this group. Thereafter, another Scandinavian country--Finland--introduced a housing allowance. Again, the allowance was designed with the intent to provide adequate housing for large households. By the late 1950s and 1960s, most Western European countries incorporated some form of housing allowance into their national housing policies.

The introduction of allowances was motived by different factors in different countries. As noted above, in Scandinavian countries housing allowances were distributed to impoverished renter households with children. In other countries, governments designed the housing allowance so that it facilitates integration of new (high cost) housing with older (lower cost) rental housing creates enough effective demand to motivate housing developers to build multifamily rental housing. Another important motivation for introducing allowances in Western Europe was to promote labor mobility. This was accomplished because subsidies are paid directly to households allowing them to shop for housing and relocate where employment opportunities exist.

Other Country Experience. In North America, both the United States and Canada use a modified housing allowance to subsidize rental housing. This is also true in Australia. South Africa, on the other hand, recently adopted a Latin American style of housing subsidy to supplement the purchasing power of lower income households and stimulate the private sector to build housing.

The United States has two versions of a housing allowance--certificates and vouchers--that assist renter households. Neither program is an entitlement program, meaning the government funds only a portion of eligible households. For both programs, housing must pass an annual inspection to determine compliance with program quality standards, and the administrative agency must determine that the rent charged by the landlord is reasonable when compared to similar units in that area.

---

[9] This section of the Annex draws from Jay Howenstine, *Housing Vouchers - A Comparative International Analysis,* Rutgers University Press, New Brunswick, New Jersey, 1986

The certificate program, created in 1974, requires households to pay 30 percent of adjusted income toward their total housing costs and the program pays the difference between the total costs and the tenant's contribution. Adjusted income for this program is gross income less deductions for dependents, excessive medical costs, child care, handicapped person care, and elderly households. Overall, the family contribution represents about 27 percent of gross income. Households must select housing with gross rents at or below a standard set for each market area based upon periodic cost surveys. If the household chooses to lease housing costing less than the standard, less subsidy is required.

The voucher program, initially implemented in 1984, provides a subsidy that is the difference between the cost of standard housing in the area the household chooses to reside and 30 percent of adjusted household income. The household may choose housing that is more or less costly than the standard. If it chooses housing costing more than the standard, it must pay the difference between the subsidy and actual cost; if it chooses housing costing less than the standard cost, the household is allowed to keep the difference.

In recent years, there have been attempts to make the two programs more alike and to consolidate them into one program. In all, there are about 1.4 million households (out of a total 33.5 million renter households) receiving this assistance throughout the country. Another 1.4 million households live in municipally owned subsidized housing. However, the U.S. Department of Housing and Urban Development is considering doing away with most producer-based housing programs and relying on housing allowances as the dominant form of housing assistance in the United States.

Eastern Europe's Recent Experience With Consumer-Based Housing Subsidies

Currently nine Eastern European countries have implemented a consumer-based housing subsidy either on a nationwide or local basis. These include Estonia, Czech Republic, Hungary, Latvia, Lithuania, Poland, Ukraine, and Russia. Slovakia will soon be added to this list. In all cases, the primary motivation for implementing a means-tested housing allowance was to protect poor households from higher housing costs associated with rent increases that generated much needed revenue for the operation and maintenance of housing.

The Czech Republic.[10] The Czech Republic has been slow to initiate reform in the housing sector after the velvet revolution. As in Slovakia, the two cornerstones of socialist housing policy--rent control and strong tenant property rights--remained in place longer than in many Eastern European countries. Although rents for existing municipal units (25 percent of the total housing stock) increased by 100 percent in mid-1992, they still remained below levels needed to cover current operating expenses and support much needed renovation. Realizing that implicit subsidies through rent control were fast accruing in the rental housing stock, the Czech government instituted a rent allowance to compensate for planned rent increases in 1994. In 1996, the government went further with housing reform by implementing a means-tested housing allowance available to all households regardless of tenure.

[10] This section of the Annex draws from published and unpublished material. Some of the information for this section came from *The Ten Commandments to the Contribution to Rent,* Ministry of Labor and Social Affairs, Czech Republic. In addition, this section draws upon conversations with Eva Holanova, Director of Income Policy, Ministry of Labor and Social Affairs for the Czech Republic.

Starting in 1994, a rent allowance was made available to all income-eligible households who lived in municipal rental or cooperative housing.[11] The rent supplement was intended to make up the difference between rent increases that took effect in 1994 and existing rent in municipal housing. In designing the rent allowance, the Czech government placed restrictions on participation in the program. Household income could not exceed 1.3 times the poverty line. In addition, a household had to prove it had payed space rent as well as costs for communal services for the previous six months. For the purpose of qualifying for the rent allowance, the average monthly income based on the previous six months was used. In addition to the rent supplement, limits were place on rent increases (40 percent, on average) from their 1993 levels. The rent allowance was also capped for all households (with a lower limit of Kc 50). The allowance was in force for a two-year period.

After one year of experimenting with the rent allowance, participation rates were extremely low due to a combination of factors. First, since the rent supplements were administered by the local social care office, they used the same income verification procedures as were in place for other social programs. This process was rather cumbersome. In addition, the rent supplement was designed so that it was last in the sequence of eligible income sources used to compute the eligibility threshold. Second, the new program was poorly advertised. Brochures were distributed to social care offices but little else was done to announce the new program. In addition, rent increases, and therefore the benefits, were too low for many eligible households to bother applying for the program. The low participation rates translated into low overall program costs. In 1994, out of the central budget allocation of Kc 1 billion for the rent supplement, only Kc 100 million was spent on actual housing expenditures (another Kc 400 million went to administration costs). In 1995, the payout for the supplement increased another Kc 100 million to reach Kc 200 million.

Starting in 1996, the Czech Republic implemented a housing allowance for owners and renters. In part, the government's motivation for introducing a housing allowance reflected the rapid price increases of utilities and rents relative to wages. Over the 1990 and 1994 period, space rents increased by about 180 percent while utilities increased by 420 percent. Wages, on the other hand, increased by only 76 percent. At the end of 1994, rent levels still needed to increase 100 to 600 percent to cover the cost of operating and maintaining public housing.

To save on administrative costs and distribute the benefits equitably--free from local political influence--the housing allowance program was integrated into the existing social safety net. Both renters and owners are eligible for housing allowances, provided their income does not exceed 1.4 multiple of the poverty line. Similar to the rent supplements, renters are eligible if they have paid their previous six months rent while owners are liable for paying property taxes. Household income, including all social benefits received during the previous quarter, is used to determine eligibility.

A complex formula is used to determine the amount of the housing allowance. It uses three parameters to determine eligibility: actual housing costs, the subsistence minimum, and household income.

$$HA = ZM(h) - \frac{ZM(h) * Y}{ZM * 1.4}$$

[11] The following discussion centers on renters since the primary purpose of the rent supplement (by definition) was to fill the gap between the rent increase that went into effect in 1994 and existing rent. Cooperative members do not in fact pay "rent" but pay the fixed amortization of the loan used to finance this type of housing. The " rent supplement" for eligible households that live in cooperatives was a flat amount varying only by household size.

Where HA represents the housing allowance; ZM(h) represents the housing cost component of the subsistence minimum; ZM represents the entire subsistence minimum, including housing costs and costs for food and clothing; and Y represents gross household income.

It is useful to rewrite the formula to better interpret its underpinnings. Simply by collecting the terms we arrive at:

$$HA = ZM(h) * [1 - ((1/1.4)*(Y/ZM))]$$

The formula shows that the benefit varies from a maximum equal to the household component of the subsistence minimum (ZM (h)), when income is zero; and a minimum of zero when income is equal to 1.4 times the subsistence minimum. Written in another way, HA = ZM(h) - ß * Y, where ß is equal to [ZM(h) / 1.4 * ZM], the formula resembles the proposed housing allowance for Slovakia, with two major deviations. First, the MSR is now simply the household component of the subsistence minimum, which varies by household size. Second, the benefit reduction rate (in the traditional formula it is the “r”) is no longer fixed, rather it varies across households according to their composition, since the subsistence minimum varies according to household size and composition. Based upon this reformulation, the value of ß decreases as the size of the subsistence minimum increases. It ranges from over 0.20 for a single adult to less than 0.10 for large households.

This benefit formula is rather unusual. The most typical design of income-tested benefit programs involves two parameters, the “guarantee” (which in our case would be the MSR), that is, the level of benefits that is guaranteed when income is equal to zero; and the “benefit reduction rate”, the rate at which benefits are reduced as income increases (which in the traditional housing allowance formula is the “r”). Together, these two parameters determine the third parameter, the “break-even point”--that is, the level of income at which the household stops being eligible for benefits.

The approach adopted by the Czech Republic reverses this logic, in that the break even point is fixed at a certain multiple of the subsistence minimum, and thus the benefit reduction rate can no longer be fixed. One of the disadvantages of this approach is to render the working of the program less understandable to the public.

Russia.[12] Russia’s starting point for housing reform was different from the majority of Eastern European countries with about 70 percent of the housing in state ownership. Accompanying this type of tenure pattern were command-economy practices that contributed to the poor quality and distribution of housing, including centralized construction methods and maintenance practices. Strict rent control applied to all public housing. Similar to other Eastern European countries, Russia quickly divested itself from its housing stock by transferring ownership of housing to municipalities. Secondly, Russia was one of the first countries to pass privatization laws that transferred title to sitting tenants in public housing at little or no cost. Housing privatization was later accompanied by institutional changes that effected the management of multi-family housing units. Following these reforms, municipalities that raised rent were required to implement a housing allowance.

In Russia a system of housing allowances was seen as a way to allow housing service price liberalization while protecting the poorer population from undue economic hardship caused by increases in housing costs. It was also viewed as a means to integrate state rental and the growing private rental sector that was not subject to rent control. With rent decontrol taking place in the public sector, rents would eventually reach parity between to two

[12] Information about Russia’s housing allowance system is found in Ray Struyk and Alexander Puzanov, *Monitoring Russia’s Early Experience with Housing Allowances,* The Urban Institute, Moscow, March 1996.

sectors causing ques for access to public housing to disappear. The magnitude of these reforms were significant since net rent in public housing had not increased since 1928. It was estimated in 1992, that revenue from net rent only covered about 25 to 30 percent of estimated maintenance needs (exclusive of deferred capital costs). In late 1992, the central government authorized municipalities to raise rents and implement a housing allowance program.

Rent liberalization was to take place over five year period allowing for implementation of a housing allowance. This program was the first means-tested program in Russia with program parameters determined at the central level though funding was the responsibility of local governments. The allowance was designed so that it would cover the gap between what a household could afford for housing and what it cost for an appropriately large standard unit. In other words, the Russian housing allowance used the formula (currently under consideration in Slovakia) HA = MSR - r * (Y). The letters MSR in this formula denote the maximum standard rent or housing costs associated with normative floor space standards. While the “r” is a coefficient that determines what a reasonable share of total household income (Y) should be attributed toward housing costs.

Central government officials designed provisions in the housing allowance that allowed for households who were overhoused to have access to smaller units with the assistance of the local governments. Given that the housing allowance formula provides a strong motivation to consume the “right” amount of housing for a given household size (because the MSR varies by household size), drafters of law were concerned that households who live in large units would be relegated to live in housing they could not afford if other (more appropriately sized) housing was unavailable. Therefore, the law mandated that local governments provide “overhoused” households with smaller units should they request to move and exempt these households from paying excess housing costs until another unit was located.

Program administration is done at the local level while some aspects of program design is dictated by the central government. This type of arrangement leads to a great deal of design variation across municipalities. For example, Gorodetz, a city of about 30,000 persons, introduced a design modification to the housing allowance that allowed the parameter “r” in the formula to vary with household income. That is, the lower the income the lower the “r” in the housing allowance formula, starting with 10 percent in the maximum case. This resulted in an increase in the number of households eligible for housing allowances. In another city, Vladimir--a city of about 350,000 people--the housing allowance formula was altered so that it could deduct “special benefits” attributed to invalids, veterans, Chernobyl victims, etc. from the MSR while keeping the benefit reduction rate or “r” in the formula constant at 10 percent. This resulted in reducing the number of households eligible for a housing allowance.

Germany.[13] Shortly, after the integration of East Germany with West Germany a housing allowance was implemented in the former socialist state. This allowance was based on the design of the allowance already in place in West Germany since 1955. East Germany had suffered the same housing problems of other countries with transitional economies including rent control, monopolistic building practices, and highly subsidized state-run management enterprises. The former state housing stock suffered from years of deferred maintenance and housing shortages associated with an arbitrary housing allocation process. Housing services were so inefficient that unsubsidized heating costs were twice as high in former East Germany than on average in West Germany. In addition, compared to West Germany, East Germany used a remarkably higher number of employees to manage and administer comparable multi-family rental housing.

---

[13] Material for this section came from *Wohngeld and Mietenbericht, 1993*, Bundesministerium fur Raumordnung, Bauwesen und Stadtebau, 1994 and personal conversation with Dr. Dick and Dr. Volker.

Eligibility for the German housing allowance is determined by a set of tables that take into account income and household size. There is no single formula for calculating the amount of the housing allowance but in theory it is intended to cover the cost of housing that might be socially acceptable. This socially acceptable level is defined by a housing costs to income ratio that on average never exceeds 28 percent. The allowance is based on rent exclusive of utilities and is limited by statutory rent ceilings. The rent ceilings vary due to: family size, local rent level, date of construction, and apartment amenities. The housing allowance is paid directly to the tenant.

By the end of 1992, about 3.8 million household in Germany were receiving a housing allowance. Approximately 1.8 million of these households lived in West Germany, or about 6 percent of all West German households. In former East Germany, approximately 2 million households or 30 percent of all households received housing allowances. By the end of 1993, the number of assisted households in former East Germany dropped to about 1.4 million due to general rise in real incomes associated with the integration process. The cost of the program in 1992 was about DM 6.8 billion, of which about DM 3.1 billion was funded by county governments; the remaining DM 3.7 billion was paid by the federal government. About 10 percent of these costs went to administering the program. In former East Germany, the housing allowance payment represented about 50 percent of all social allowances payments.

In conjunction with the introduction of the housing allowance, rent and utilities in former East Germany increased by 400 percent from 1991 to 1992. Without the allowance, this rent increase would have caused households with low incomes to pay about 30 percent of their income towards housing costs. But with the allowance in place, the average housing cost-to-income ratio dropped to about 20 percent. By 1992, about 31 percent of all tenants were receiving a housing allowance with an average payment of DM 105 per month. The average share of income devoted to housing costs for housing allowance recipients in former East Germany was 18.3 percent while for non-recipients--even with a 400 percent increase in housing costs--the share was only 16.7 percent.

The introduction of a housing allowance combined with other reforms has had a positive impact on afford ability, levels of investment, and household mobility in former East Germany. As early as 1992, the level of investment in the housing sector started to increase, especially among renter households who chose to rehabilitate their housing. In 1993, the number of building permits for rehabilitation increased by about 70 percent over the previous year. Over this same period, new housing starts increased by about 31 percent causing residential construction to be the fastest growing sector in former East Germany. Heating costs (excluded from the housing allowance) have also decreased due to a program of metering individual apartments. Whereas household mobility was stifled in the communist era, survey results show that, in 1993, about 11 percent of all households planned to move within two years while another 9 percent considered it very likely that they would relocate.

Ukraine.[14] Since the Ukraine was part of the former Soviet Union, it housing stock suffered from the same problems associated with socialist provision of housing. Price liberalization has proceeded at a slower pace than in the rest of Eastern Europe. By 1994 housing subsidies amounted to about three-quarters of the national budget deficit. In order to qualify for financial assistance from international agencies, the government agreed to cut subsidies to reduce the budget deficit which had grown to about 20 percent of all government expenditures in 1994. Rapid increases of the price of housing services, including utilities, were necessary to reduce the deficit and increase revenue for much needed housing maintenance and repair.

[14] Information for this section on the Ukrainian system of housing allowances came from Roger Vaughan, *A History and Overview of Ukraine's Housing Subsidy Program,* PADCO, Kiev, Ukraine, November 1995.

The design of the Ukraine housing allowance was extremely simple, reflecting the need to implement the program quickly. The housing allowance paid subsidies to households if their total monthly housing payments exceeded 15 percent of their average gross income during the preceding three months. The subsidy was based on a payment structure that allowed 21 square meters per person as a norm in order to avoid paying disproportionately large subsidies to households that lived in apartments larger than the norm. To facilitate income verification, the housing allowance was only paid to those households in which all adults were either working or looking after disabled household members, or were registered as an unemployed worker or student.

With a housing allowance program in place, the government of Ukraine was able to increase prices of housing and utilities to cover about 40 percent of their costs. With lower incomes than generally found elsewhere in Eastern Europe (average of $50 per month), Ukraine households were particularly vulnerable to increases in expenditures for rent and utilities. Without the housing allowances, one half of all households would have had to pay more that 50 percent of their income towards housing costs.

Since the allowance program had to be implemented quickly, the government (assisted by USAID) spent a great deal of resources to set up the apparatus to administer the new social program. About 4,000 new employees were hired and trained over a three-month period using training materials that included a manual and a video. Copies of these materials were distributed to 750 housing allowance offices throughout the Ukraine. In May 1995, these new offices began taking applications for housing allowances and verifying the income of applicants. Office staff used custom computer software to assist with intake and monitoring. In addition, a wide-scale public information campaign was launched using television advertisements, radio commercials, and printed poster boards.

By the fall of 1995, about 800,000 Ukrainian households were receiving housing allowances. This represented about 5 percent of all households; about 6 percent of all households applied for the benefits. About 81 percent of these applicants were from urban portions of the country. The total cost of the program was much less than the government anticipated since its projections were based on 100 percent participation rates among eligible households. The total cost of the program in the first year was $28 million while the budget deficit was reduced by about $600 million due to reductions in subsidies resulting directly from the program of housing allowances.

Other Eastern European Countries. Less information is available about other housing allowance programs in Eastern Europe. Estonia and Lithuania, at one time, utilized a housing allowance that takes into consideration the number of household members and income. The allowable share of income spent on housing is higher for higher income households. Rent liberalization has been particularly rapid in these countries despite the fact that their incomes are somewhat lower, on average, than most of the other Eastern European countries.

Poland introduced a housing allowance in 1995. Survey data there show that a large share of the richest urban households occupy rent-controlled housing. New rental legislation will allow rents to rise to cover the full cost of operating and maintaining housing. As of 1995, rents only covered about 35 percent of operation and maintenance costs. Public and private housing renters and cooperative owners are eligible for allowances. Income eligibility for the new allowance is set at the pension level and the maximum share of income devoted to housing varies by household size (i.e., 15 percent for single person households, 12 percent for 2 to 4 person households, and 10 percent for all other households).

Although Hungary does not have a nationwide housing allowance program, localities implement housing allowance programs. With USAID technical assistance, the city of Szolnok implemented a housing allowance program. The city increased rents, introduced housing allowances, and reformed its municipal housing management practices. The design of the housing allowance was based on the same formula proposed for Slovakia, that is, the allowance covered the gap between what a household could afford and the normative cost of standard quality housing. The city set the maximum share of income devoted toward housing cost at 35 percent of gross income. For renters, the maximum standard rent included space rent and utility costs. For homeowners, there was a separate utility allowance with an additional subsidy to cover mortgage payments. Less than half of all eligible households participate in the housing allowance program. About 42 percent of all eligible households participated in the program during the first two years.

ANNEX B